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Research Bulletin

# *Repurchasing Common Stock*

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# Overview

It seems paradoxical for strong, growing corporations to enter the stock market to buy back their own common shares. Nevertheless, there can be sound business reasons for doing so. Many companies, and there are substantial numbers of them, have continuing needs for a supply of shares for various corporate programs. And they may not wish to satisfy these demands by distributing new, previously unissued shares. In such cases, the alternative is to buy back shares in the open market.

When the market prices of their shares become depressed, as a large number were for many months prior to August, 1982, the managements of some corporations see favorable profit opportunities because they are confident that their companies' share prices will eventually recover. These, and other reasons to be discussed later, influence companies to repurchase their own shares.

The purpose of this study is to examine the phenomenon of corporate stock repurchasing and to seek answers to such questions as:

—What do company managements hope to accomplish by repurchasing their stock? To what extent have their expectations been realized? And do they intend to continue?

—To what extent have the reduced numbers of shares outstanding increased earnings per share and enhanced the market value of remaining outstanding shares? In other words, can enough shares be reacquired by a large corporation to make any difference in these measurements of corporate financial health?

—What policy guidelines and procedures have companies installed to administer their stock repurchasing programs? Which executives are responsible for conducting these programs?

In earlier studies of corporate stock-repurchasing practices, attention has typically been centered exclusively on programs for corporations to go directly into the markets and repurchase shares that are accounted for simply as treasury stock in the companies' financial statements. However, another aspect of repurchasing is worthy of attention. Numerous corporations operate employee-benefit programs such as stock-purchase plans and profit-sharing trusts. These and similar activities require the investment of the programs' assets in shares of the sponsoring company. In some cases, the effects on the company of such indirect repurchasing activities can be similar to those of the more commonly recognized direct stock repurchasing programs.

Subsequent sections of this report examine company experience with both direct and indirect repurchasing of common stock.

**Background of this Report**

In the early 1970's, the practice of corporations buying back substantial quantities of their own common stock surged to a previously unheard of peak of activity. Responding to requests from its Associates for information concerning this development, The Conference Board issued a report in 1975.[1] Although the number of large corporations repurchasing their own shares has declined somewhat in the past ten years, the total volume of shares reacquired has grown substantially. In brief, common stock repurchasing has remained a significant feature in the conduct of many large corporations' financial affairs.

As part of its continuing study of corporate financial management practices, the Board has reexamined the phenomenon of common stock repurchasing. This report updates a major portion of the findings reported in 1975. In addition, it examines a facet of stock repurchasing that was not considered in the earlier study: indirect repurchasing by various employee benefit programs, such as employee stock-ownership plans, profit-sharing trusts, and the like.

[1]Francis J. Walsh, Jr., *Repurchasing Common Stock*. The Conference Board, Report No. 659, 1975.

## Extent of Repurchasing Activity

In recent years, corporations whose common shares are listed on the New York Stock Exchange (NYSE) have been repurchasing in excess of 100 million shares annually, as shown in Table 1. In the first ten months of 1982, according to NYSE data, 107 listed companies repurchased 100,000 shares or more; and 25 of these bought back 1 million or more shares. The total number of shares acquired by 297 companies in the first 10 months of 1982 was 218.9 million, and this was a substantial increase over the 148.4 million shares reported by 312 firms for the full year of 1981, and 101.3 million by 305 corporations in 1980. The sharp increase in 1982 volume undoubtedly reflected the generally depressed condition of stock market prices prior to the recovery that began in August, 1982, and it demonstrates the determination of many repurchasing companies to exploit favorable buying opportunities.

The 1975 Conference Board study of common stock repurchasing reported that there was a great increase in this activity in the period from 1969 through 1973; the latter year witnessed the reacquisition of 143.8 million shares by 522 companies.[1] Since 1980, the volume of repurchased shares has increased substantially. The number of firms engaging in repurchasing, however, has remained basically stable.

Most companies that engage in repurchasing do so to acquire shares for disposition within a fairly short time

[1]Francis J. Walsh, Jr., *Repurchasing Common Stock*. The Conference Board, Report No. 659, 1975.

**Table 1: Summary Data on Stock Repurchases**

| | 1973 | 1980 | 1981 | 1982[a] |
|---|---|---|---|---|
| Companies reporting purchases | 522 | 305 | 312 | 297 |
| Companies purchasing 100,000 shares or more | 219 | 134 | 113 | 107 |
| Number of firms purchasing 1 million shares or more | 32 | 20 | 32 | 25 |
| Shares acquired (millions) | 143.8 | 101.3 | 148.4 | 218.9 |
| Largest purchaser (millions) | 13.1 (Gulf Oil) | 12.5 (Standard Oil Indiana) | 26.4 (Exxon) | 14.1 (Brunswick) |

[a]Data cover only first 10 months of 1982.

Source: *Fact Sheets*, New York Stock Exchange, January, 1980; October, 1982. Also Francis J. Walsh, Jr., *Repurchasing Common Stock*. The Conference Board, Report No. 659, 1975.

period (e.g., for distribution to employee stock-purchase-plan participants or to acquire other corporations). Nevertheless, during the period of time that the corporation holds the repurchased shares, it must account for them as treasury stock.[2] Some firms may hold a substantial portion of their capital stock in the treasury for a time, as shown in Table 2.

## How This Study Was Conducted

Some aspects of corporate securities repurchasing were specifically excluded from this study. For example:

- From time to time, a company's management decides to "go private," and offers to repurchase all of the shares held by the general public. After the repurchase, the remaining outstanding shares are held by only a few individuals and are no longer actively traded. Some companies that issued common stock to the public during the long bull market that ended in the late 1960's later offered to repurchase these shares when the market prices of their securities declined sharply. This practice elicited strong criticism from the Securities and Exchange Commission (SEC). Such companies were not included in this study. The aim here is to examine the practices of larger corporations that continue to be publicly owned and that repurchase shares for reasons other than going private.
- The practices of companies that repurchase debt instruments or preferred stock are also specifically excluded.

### *Questionnaires*

In order to obtain information about common stock repurchasing, two questionnaires were addressed to the chief financial executives of a group of major corporations.

The first questionnaire was directed to 113 corporations whose capital stocks are listed on the New York Stock Exchange (NYSE) and that repurchased 100,000 shares or more during 1981, as shown by NYSE tabulations of repurchasing activity. A total of 72 of these firms (64 percent of those invited to participate) provided usable data. Some of these respondents were also interviewed (in person or by telephone) to obtain additional information.

The second survey was addressed to a group of companies that did not engage in direct repurchasing of treasury stock. Rather, their common shares were purchased as investments of the funds of various employee benefit plans, such as employee stock-ownership programs and profit-sharing trusts. Such indirect purchases, although not counted as treasury stock by the corporations sponsoring the benefit programs, nevertheless bring substantial quantities of shares under the effective control of the companies.

New York Stock Exchange listed corporations also were selected for this second questionnaire. However, companies that were known to be direct purchasers of their own shares (as indicated by the NYSE repurchasing tabulations) were excluded from consideration. From the remaining NYSE listed corporations, a group of 200 randomly selected firms was surveyed. Sixty-two com-

**Table 2: Shares of Capital Stock Held as Treasury Shares, 1981**

| Percent Held by Company | Number of Companies |
|---|---|
| 40.1%-and more | 4 |
| 35.1-40.0 | 4 |
| 30.1-35.0 | 3 |
| 25.1-30.0 | 9 |
| 20.1-25.0 | 7 |
| 15.1-20.0 | 16 |
| 10.1-15.0 | 24 |
| Under 10.0 | 321 |
| Total | 388 |

Source: *Fact Sheets*, New York Stock Exchange, January, 1980; October, 1982.

[2]The accounting treatment of treasury stock was described in Walsh, Chapter 4.

panies (31 percent) supplied information in response to this second inquiry. In all, 134 corporations took part in this study.

### The Climate for Repurchasing

General business conditions, and more specifically the state of the stock market, are claimed to influence the timing and amounts of common stock repurchases. For example, more than one-fourth of the participants report that they try to purchase shares aggressively when market prices are low or are considered to be undervalued. Other firms are guided more by their current needs for shares, and they repurchase as needed to meet the demand. And another sizable group repurchases on a steady, continuing basis regardless of external conditions.

Internal conditions also influence the climate for repurchasing. Availability of cash, for example, and the lack of presently attractive alternative uses of funds prompt some companies to buy back some of their outstanding shares.

The following tabulation summarizes the circumstances that influence direct common-stock repurchasing activity in the 69 companies that supplied such information:

| | *Percent of Responses* |
|---|---|
| Purchase stock aggressively when stock market prices depressed | 28% |
| Purchase stock on an ad hoc basis, depending on current needs | 23 |
| Purchase stock on regular, year-to-year basis, irrespective of stock market conditions | 22 |
| Purchase stock aggressively when cash flows are large, and there is no higher priority use of funds | 16 |
| Purchase stock aggressively when business conditions are weak and investment projects can be deferred | 2 |
| Other[1] | 10 |
| | 100%[a] |

[1]Includes: purchase of stock based on favorable long-term trends; purchases timed to minimize average cost per share; exchange of shares on exercise of options; repurchase of stock from resigning employees; special situations only; and when large blocks become available.

[a]Details do not add to 100 percent because of rounding.

According to executives who took part in this study, tax and regulatory legislation in recent years have influenced the volume of indirect repurchasing of company stock by benefit programs. The Employee Retirement Income Security Act (ERISA) of 1974 and various tax bills enacted by Congress have served to encourage establishment of benefit programs that invest varying proportions of their assets in sponsoring companies' shares. The Profit Sharing Research Foundation (Evanston, Illinois) reports that more than 723,000 benefit plans of this type were approved between 1975 (when ERISA went into effect) and 1981.

### Profile of Companies Studied

Three out of four of the seventy-two NYSE-listed corporations that supplied usable information on their direct stock-repurchasing programs are primarily in the manufacturing sector of the economy. Durable goods manufacturers make up the largest single segment, with 41 percent of all of the survey participants. Nondurable goods manufacturers represent 35 percent of the total; nonmanufacturing enterprises account for the remainder.

Large corporations tend to predominate among the companies that engage in direct stock repurchasing. Sixty-four percent of the survey participants have sales volumes in excess of $1 billion. At the opposite end of the spectrum, only 5 percent of the respondents have annual sales of less than $100 million.

Manufacturing companies also make up the bulk of the 62 respondents supplying information about indirect repurchasing of capital stock through their benefit programs. Seventy-two percent of these companies are in the manufacturing sector (37 percent durable goods and 35 percent nondurable goods). The remaining 28 percent are nonmanufacturers.

There is a somewhat broader distribution as to company size among this second group of cooperators than there is among the direct repurchasers described above. Forty-eight percent reported annual sales volumes of $1 billion or more. But, medium-sized firms are more widely represented, with 18 percent of the companies in the $500 million to $1 billion bracket and 31 percent in the $100 million to $500 million category. Again, smaller corporations are very much in the minority, with only 3 percent reporting sales of less than $100 million.

# Direct Repurchasing of Common Stock by Corporations

The most important common stock repurchasing activity is carried on directly by company managements in pursuit of specific corporate objectives. This aspect of repurchasing, described in this section, is based primarily on information supplied by 72 corporations that are listed on the New York Stock Exchange and that were substantial direct repurchasers of their own shares during the five-year period beginning in 1978 and ending in 1982.

These 72 corporations are not merely casual or occasional repurchasers. Close to eight out of ten acquired treasury shares in each of the five years (1978-1982). As the following tabulation shows, two out of three increased their holdings during the period:

| *Holdings of Treasury Shares (1978-1982)* | *Number of Companies* |
|---|---|
| Large increase | 20 |
| Small increase | 28 |
| Little or no change | 8 |
| Decrease | 13 |
| No shares held at end of period | 3 |
| Total | 72 |

The 20 companies reporting large increases typically added one million or more treasury shares. One firm added 13 million shares to its holdings, while two others reported increases of 6.5 million shares and 4 million shares, respectively.

## Objectives

Although more than a dozen objectives of common-stock repurchasing are mentioned by the participating companies, (see Table 3), four stand out for both frequency of mention and relative importance (when ranked):

—Obtaining shares for employee compensation programs;
—Exploiting investment opportunities presented by depressed stock prices;
—Improving earnings per share;
—Obtaining shares for acquisition programs.

*Incentive Compensation, Stock Options, and Stock-Purchase Plans:* The most frequently chosen "important" motive for reacquiring common stock is obtaining shares for reissue to executives and employees under various compensation, stock-option, and stock-purchase plans.[3] Sixty-four firms cited this as an objective of their repurchasing programs. And, as indicated in Table 3, 38 firms ranked it first in importance.

*Exploiting Investment Opportunities:* When the market price of a company's capital stock appears to be temporarily depressed, there is a strong incentive for

[3]For recent experience with stock option plans, see Harland Fox, *Incentive Stock Option Plans.* The Conference Board, Research Bulletin No. 148, 1983.

**Table 3: Principal Objectives of Direct Common Stock Repurchasing Programs, Ranked by 72 Companies**

| | *Rank* | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| | *1* | *2* | *3* | *4* | *5* | *6* | *7* | *8* | *Total Mentions*[1] |
| | *Number of Times Listed* | | | | | | | | |
| Obtaining shares for employee compensation programs | 38 | 9 | 8 | 4 | 3 | 2 | | | 64 |
| Exploiting the investment opportunity | 17 | 10 | 5 | 4 | 3 | 1 | | | 40 |
| Improving earnings per share | 2 | 7 | 10 | 2 | 3 | 1 | 1 | | 26 |
| Obtaining shares for acquisitions | 2 | 6 | 8 | 6 | 1 | | 2 | | 25 |
| General corporate purposes (unspecified) | 3 | 9 | 6 | 1 | 3 | 1 | | | 23 |
| Obtaining shares for conversion | | 12 | 1 | 1 | 1 | | | 1 | 16 |
| Preventing dilution | 3 | 4 | 5 | 2 | | 1 | 1 | | 16 |
| Supporting market price | 2 | 4 | 3 | | 1 | 1 | | | 11 |
| Increasing book value | | 1 | 3 | 5 | 2 | | | | 11 |
| Changing ratio of debt to equity | 1 | 2 | 1 | 1 | 2 | | 1 | | 8 |
| Temporary investment of cash | | 1 | 1 | 4 | 1 | 1 | | | 8 |
| Preventing unwanted takeover | 3 | 1 | 2 | 1 | | | | | 7 |
| Reducing cost of servicing small stockholder | 1 | | 3 | 1 | | | | | 5 |

[1]Multiple responses.

management to buy some of these shares for the company treasury. Executives who are confident that the price of their company's stock will rebound believe such purchases to be one of their best investment opportunities. Frequently, the firm may have other purposes in mind for acquiring shares (e.g., the compensation plans mentioned above); but they try to time their repurchases to take advantage of bargain prices in the market. Seventeen respondents rated this objective as most important.

*Improving Earnings per Share:* Earnings per share of common stock (EPS) is a financial indicator of company performance that is closely watched by shareholders and by the investment community in general. It is computed simply by dividing a company's net income for a period of time by the average number of shares outstanding during that period.[4] Shares held in the company treasury do not count as "outstanding"; therefore, a company can automatically improve its reported EPS by buying up its own common shares.

Twenty-six companies mentioned this as an objective of their repurchasing programs. However, only two rated it as their most important objective.

*Acquisition Programs:* Corporations that acquire other companies frequently do so by issuing shares of stock in exchange for the outstanding shares of the acquired company. Obtaining shares of their own stock for the purpose of making such deals is a frequently cited objective of stock repurchasing programs. Twenty-five participating companies reported this as an objective, but only two gave it first rank.

*Conversions:* Issuance of convertible securities (such as debentures and preferred stock) can be somewhat troublesome for the issuing corporation because it dilutes the equity position of the present stockholders. Such dilution occurs when the corporation must issue new shares of common stock to meet the demands of security holders who wish to exercise their conversion privileges.

One way to get around this problem is to repurchase shares of common stock that are already outstanding and hold them in the treasury until the convertible securities are turned in. Sixteen companies report this practice as an objective of their repurchasing programs but none ranked it first in importance.

*Preventing Dilution:* Closely related to the two previous aims is the objective of preventing dilution of the present stockholders' equity interest in the company. By repurchasing some of the common shares that may have been issued recently for a variety of purposes, some managements strive to preserve the ownership interest of important groups of stockholders. Twelve of the sixteen companies reporting this objective rank it first, second or third in importance. (The questionnaire listed 17 possibilities.)

*Supporting Market Price:* It has long been held that a basic reason for repurchasing stock is to prevent the market prices of company shares from sliding to a level that is lower, perhaps, than the book value of the company. There is some doubt, however, as to the ability of big companies, with large amounts of stock outstanding, to buy back enough of their own shares to make much difference in the market price. Futhermore, some executives believe that it would be illegal to engage in this practice, even if it were possible to influence market prices. Nevertheless, eleven companies cited market price support as an objective of repurchasing, and nine of them ranked it first, second or third.

*Increasing Book Value:* Some security analysts are interested in a corporation's book value: the stockholders' equity total, as it appears on the balance sheet, divided by the number of shares outstanding. If a company buys back some of its shares, it may be able to increase the book value.

To achieve this goal fully, however, the repurchased shares must be retired. Otherwise, these shares are simply reported as treasury stock on the balance sheet and the amount invested therein is deducted from the stockholders' equity total. Thus, the numerator of the fraction is reduced concurrently with the number of shares reported as outstanding, and there may be little or no net effect on the resulting book value per share. Although 11 companies reported this as an objective, most of them did not give it a very high rank.

*Changing Ratio of Debt to Equity:* The relationship between a company's total debt and its total stockholders' equity is an important indicator of a firm's basic financing policy. Generally, a company with a lot of debt compared with the owners' equity is considered to be somewhat risky. On the other hand, a low proportion of debt may be regarded as too conservative in the sense that the stockholders are denied the advantage of leverage.

To some extent, a firm that wishes to do so can increase its ratio of debt to equity by repurchasing some of its common stock. Eight participating companies reported this as an objective of their repurchasing programs and half of them ranked it first, second or third in importance.

*Temporary Investment:* Companies with temporary cash surpluses sometimes invest some of this cash in their own common stock. Eight companies that responded to the survey report that temporary investment of surplus cash is an objective of their repurchasing programs. None of them gave it a very high ranking, however.

*Preventing Unwanted Takeovers:* Managements that

[4]This computation may become complicated when a company issues other classes or types of securities that are potentially convertible into shares of common stock. However, such complexities do not affect the rationale for repurchasing stock for the purpose of improving EPS.

believe their firms are actual or potential targets for acquisition by other corporations may engage in stock repurchasing as a defensive measure. By removing some shares from the market, they increase the proportion of stock controlled by the present management. Seven companies reported this as an objective of repurchasing programs, and six of them ranked it among the top three in importance. Thus, when it is an objective, it is an important one.

*Reducing Cost of Servicing Small Stockholders:* When company stock is held by large numbers of small shareholders, financial executives may feel that the cost of servicing small shareholder accounts is a financial burden. Therefore, they may encourage the practice of buying back shares from small shareholders. Five companies participating in the study reported this as an objective, although only one of them ranked it as first in importance.

*Other Objectives:* Other objectives of common stock repurchasing, reported by only two or three companies each, are:

- Acquiring shares to contribute to the pension fund;
- Retirement of shares; and
- Partial liquidation of the business because of reduced need for capital.

## Results of Repurchasing

Were these companies generally successful or unsucessful in achieving their aims? What problems or pitfalls did they encounter?

### Degree of Success Achieved

Stock repurchasing generally has been successful for most of the respondents. A high or moderate degree of success was reported by companies for the majority of objectives. A high degree of success generally was achieved for ten of them:

| *Objective* | *Percent of Respondents Reporting a High Degree of Success* |
|---|---|
| Stock options, incentive compensation, and stock-purchase plans | 89% |
| Conversion of other securities | 88 |
| Preventing dilution of equity | 71 |
| Acquisition programs | 68 |
| Exploitation of bargain prices | 60 |
| General corporate purposes | 48 |
| Improving earnings per share | 46 |
| Increasing book value per share | 46 |
| Reducing cost of servicing small stockholders | 40 |
| Preventing unwanted takeover attempts | 33 |

In addition, the respondents reported a moderate degree of success with these objectives:

| *Objective* | *Percent of Respondents Reporting Moderate Success* |
|---|---|
| Increasing ratio of debt to equity | 75% |
| Temporary investment of surplus cash | 75 |
| Supporting the market price | 73 |
| Preventing unwanted takeover attempts | 67 |
| Reducing cost of servicing small stockholders | 60 |
| Increasing book value per share | 54 |
| Improving earnings per share | 54 |
| General corporate purposes | 52 |
| Exploiting bargain prices | 38 |

To sum up, the most frequently mentioned objectives of stock repurchasing, and those considered most important by companies taking part in this study, are generally judged highly or moderately successful when overall results are weighed.

### Problems and Pitfalls

Despite the generally favorable results, stock repurchasing programs are not unmixed blessings. There are disappointments and problems as well.

For example, efforts to exploit bargain prices in the market produced lackluster results for some companies because of the prolonged period of stock market weakness in 1981 and 1982. When the prices of the shares failed to rise within a reasonable time frame, the shares did not seem to be such a bargain after all.

Attempts to support the market prices of company shares similarly proved to be rather unsuccessful. When asked if they could identify any changes in the market prices of their shares as a direct consequence of stock repurchasing, 58 participants (81 percent of the total) reported no discernible change. Seventeen percent noted a slight increase; and only one respondent perceived a significant increase.

Then, too, some executives do not really believe that repurchasing the company's own shares is a wise use of corporate cash. They feel that such investments divert resources that might better be used in the companies' principal operations. Also, executives who have conservative attitudes toward capital structures do not consider it wise to reduce the shareholders' equity, as repurchasing does.

Legal problems are occasionally also cited. For example, one company reported a stockholder suit that arose from stock repurchasing. Another mentioned compliance with SEC rules as a difficulty.

SEC rules cover two broad areas insofar as stock repurchasing is concerned. The first area has to do with disclosures concerning the effects on earnings and capitalization. The following disclosures are required:

(1) Effect of repurchasing on earnings per share.
(2) Effect of repurchasing on the trend in earnings.
(3) Effect of repurchasing on company capitalization, specifically the effect on the debt-to-equity ratio.

The second area of SEC rule making is designed to prevent maneuvers that could influence the price of a company's stock. New rules concerning market transactions were first proposed in 1981; revisions were announced on November 17, 1982, under SEC Rule 10b-18. In effect, Rule 10b-18 provides a safe harbor from liability for manipulation in connection with purchases by an issuer of its own common stock. The SEC, in this Rule, intends to limit the volume, timing, pricing and method of stock repurchases so that an issuer would be required to follow the market, rather than to lead it. In general, the Rule:

(1) Limits a company to placing an order with only one dealer-broker on any given day. This prevents creating the illusion of widespread demand.
(2) Prohibits buying stock prior to an independent purchase, and also prohibits such buying within 30 minutes of the close of the market. This avoids influencing the opening and closing prices.
(3) Limits bidding for stock by the company to the highest independent bid. This prevents the bidding company from leading the market.
(4) Restricts volume on any day to 25 percent of the average daily trading volume of the previous four weeks. This prevents market domination by the repurchasing company.

### Repurchasing Plans

Evidence of general satisfaction with their direct stock repurchasing programs can be seen from the responses of participants with respect to their plans to continue repurchasing. Forty-six companies, or 64 percent of the total, declare their intention to continue. Only 12 firms (17 percent) say they do not plan any more repurchasing. The remaining 14 respondents are undecided at this point.

The principal reason why the majority plans to continue repurchasing is the need for a steady supply of shares to meet the demands of compensation, stock-option and stock-purchase plans—the most important objective of most repurchasing programs. Another compelling reason for some firms to continue repurchasing is that they consider their shares still undervalued in the stock market. And other companies expect a continuing need to obtain shares for acquisitions, or to respond to other special situations.

Sixteen percent of the respondents' companies do not intend to carry out any further repurchasing in the near future. The reasons given for this decision are:

—Availability of preferable investment alternatives;
—Restrictions in loan agreements;
—Use of internal cash flow to achieve objectives;
—Balance sheet at desired position regarding debt-to-equity relationship.

Some 20 percent of the participating companies are undecided about whether they will continue repurchasing their own common stock. A large manufacturer of durable equipment notes: "Repurchase will depend on future availability of funds for this type of investment, as well as market price, book value, loan covenants, and other external factors." A large firm in the forest products industry indicated that stock repurchase "depends upon price of stock, financial outlook, and other investment opportunities." In general, the companies indicating they are undecided have been satisfied with past repurchases, and have evaluated their repurchase programs as "highly" or "moderately" successful.

## Administration of Direct Repurchasing Programs

The group of companies participating in this study includes some that have been repurchasing shares for many years. In such cases, they have developed well-established and carefully detailed administrative procedures for purchasing stock. Other companies have only recently introduced stock repurchase programs, or only occasionally engage in stock repurchasing. The companies that supplied information for this study belong mainly in the first group.

The administrative matters on which the surveyed companies were asked to furnish information are:

—Timing of purchases (continuous or irregular);
—Methods of obtaining shares;
—Assignment of responsibility for programs; and
—Use of written guidelines for repurchasing.

### Timing

Slightly more than two out of three of the responding companies repurchase their shares only at irregular intervals. The remainder have continuous, or ongoing, programs.

The majority repurchasing on an irregular, ad hoc basis tend to buy larger quantities of shares at a time, and then to hold them in the company treasury for disposal as needed. Although a company might need a supply of shares on a fairly continuous basis, the financial managers may prefer to time their repurchasing activities so as to exploit favorable buying opportunities.

Companies with continuous repurchasing programs usually have an ongoing and predictable need for a supply of shares and, therefore, they have standing arrangements to buy on a daily, weekly or other periodic basis. They can also minimize any criticisms of their programs (e.g., attempting to manipulate prices) and they avoid disturbing the markets for their shares.

### How Shares Are Acquired

Purchases through brokers is the method of repurchasing utilized by three out of four respondents supplying information on this point. In the case of such market purchases through brokers, SEC guidelines call for the use of only a single broker, and several companies referred to this practice in providing information for this study. Frequency of use of various methods of purchasing stock is tabulated below:

| *Method* | *Number of Times Mentioned*[1] |
|---|---|
| Purchases through brokers | 55 |
| Direct purchases of shares offered by individuals or by holders of large blocks of stock | 39 |
| Tender offers | 9 |
| Purchases from employees who acquired shares through savings plans | 9 |
| Exchange offers | 3 |
| Purchases through banks that obtain shares through savings plans | 1 |
| Other | 3 |

[1]Multiple responses.

Over 40 companies that provided information on this point use more than one method to reacquire common stock. The most frequent alternative to use of brokers is direct purchase of shares offered by individuals or holders of large blocks of stock.

Tender offers may be somewhat more costly than acquiring shares through a broker purchasing in the open market. However, tender offers provide the company with the offsetting advantage of being able to complete the acquisition of stock within a relatively short span of time, therefore minimizing risks of market fluctuations.

Occasionally, stockholders offer to sell their shares to the company, and many companies appear to be ready to buy whatever shares become available. At times, large blocks of stock become available via this route. In such cases, it is helpful for companies to be immediately aware of such offerings, since they represent a potential overhang on the market which could discourage some investor interest and lead to a decline in the price of the company's shares.

### Responsible Executives

As might be expected, financial executives, with a variety of job titles, are generally assigned the responsibility for administering stock repurchasing programs.[3] Treasurer is the title most frequently encountered, with more than half of the survey participants reporting the repurchasing administrator as having a title that includes "treasurer."

The following tabulation summarizes the various job titles reported by participants:

| *Title* | | *Number of Mentions*[1] |
|---|---|---|
| Treasurer | 20 | |
| Vice president and treasurer | 19 | |
| Assistant treasurer | 7 | 46 |
| Vice president, finance and/or chief financial officer | | 16 |
| Chairman or president | | 3 |
| Secretary | | 3 |
| All others (mentioned once each) | | 16 |

[1]Multiple responses.

### Written Guidelines

More than half of the companies supplying information on this subject have prepared some form of written guidelines for their stock repurchasing activities. These guidelines appear in a variety of forms:

—Resolutions of the board of directors;
—Minutes of board committee meetings;
—Letters of authorization and instruction addressed to stockbrokers;
—Statements of financial policy or procedure.

An example of a corporate procedure statement appears in Exhibit 1. Several companies, either in addition to or in lieu of their own written statements, adopt the SEC rules described above (page 9) as their policy guidelines.

[3]For a detailed description of corporate financial executives and their titles, see Patrick J. Davey, *New Patterns in Organizing for Financial Management*. The Conference Board, Report No. 839, 1983.

**Exhibit 1: Administrative Procedure—A Major Industrial Company**

**Subject: Acquisition and Disposition of Treasury Stock**

I. General

The purpose of this procedure is to document the various sources and uses of treasury stock, and describe procedures for acquiring and disposing of shares to the extent that Banking and Corporate Finance is responsible.

II. Acquisition of Treasury Stock

Treasury stock is acquired principally from direct purchase, either (1) through a securities dealer in the open market, or (2) from employees under the Company's stock redemption program. A small portion of stock is also acquired through repurchase of shares returned by the Stock Bonus and Employee Stock Ownership Plan Trusts.

III. Disposition of Treasury Stock

Treasury stock is disposed of principally by transfer to (1) Savings and Security and Stock Bonus Trusts, (2) Employee Stock Ownership Plan Trust, or (3) Treasury Operations (Securities Transfer Operation) for Incentive Compensation and Stock Option Plan requirements. Other periodic uses of Treasury stock include corporate acquisitions and bond conversions.

IV. Authority

Authority for acquisitions and dispositions of Company stock for employee plan purposes is established annually by the Board of Directors through adoption of a stock purchasing program as requested in a letter prepared by Corporate Treasury for the Board's Finance Committee. Responsibility for administering the program has been assigned to Corporate Treasury Operation, and attendant authority to contract for open-market purchases is delegated by Board Resolution to the Vice President and Treasurer or Manager-Banking and Corporate Finance.

Any stock to be used for Company acquisitions will be authorized by specific Board Resolution. Any transfer of shares for bond conversions as authorized by the Board of Directors Resolutions dated May 26, 1972 and May 25, 1973 will be approved by the Treasurer and/or the Manager-Foreign Financing.

V. Open-Market Purchases

Purchases on the open market will be made through established securities firms as authorized by the Manager-Banking and Corporate Finance, and will be made in compliance with Securities and Exchange Commission regulations governing stock repurchases (presently Rule 10b-18).

Arrangements with firms will be confirmed in writing concerning daily quantities to be purchased, agreed upon commission rates, daily reporting, delivery of shares to custody, and compliance with SEC regulations. Securities firms will be instructed to deliver all shares on settlement date (five business days following purchase) to [Bank], Custodian. The bank, in turn, will be authorized in writing daily concerning (1) the number of shares to be accepted, (2) the exact dollar amount to pay to the delivering firm and charge to the Treasurer's account, and (3) delivery of shares for registration. These letters will be signed and countersigned by individuals authorized by Board Resolution. Copies will be forwarded to the Manager-Cash Operations (for bank account reconciliation) and to the Manager-Accounting Operations (for ledger maintenance and reconciliation). Confirmation advices received from securities firms will be reviewed by the Secretary to the Manager-Corporate Investment as received to verify that they agree in all respects with information previously given to the bank.

VI. Purchases from Employees under Stock Redemption Program

This program is administered by Employee Savings Operation. Banking and Corporate Finance will be notified of the number of shares redeemed via copies of Employee Savings Operation's transmittal letters to Securities Transfer Operation requesting re-registration and delivery to custody at the bank.

VII. Repurchases from Stock Bonus Trust

Upon acquisition of shares of stock from participants in the Stock Bonus Plan in settlement of vested fractional shares, the Trust will offer to sell the shares to the Company at the closing market price per share on the New York Stock Exchange on the date of sale. The offer will be accepted on behalf of the Company by the Manager-Banking and Corporate Finance. Banking and Corporate Finance will then authorize the Custodian Bank in writing concerning (1) the number of shares to be accepted from the Custodian for the Trust, (2) the exact dollar amount to be paid and charged to the Treasurer's account, and (3) delivery of shares to Securities Transfer Operation where they will be registered in the name of the Company and then returned to the bank for custody. This letter will be signed and countersigned by individuals authorized by Board Resolution. Copies will be forwarded to the Manager-Cash Operations (for bank account reconciliation) and the Manager-Accounting Operations (for ledger maintenance and reconciliation).

**Exhibit 1: Administrative Procedure—A Major Industrial Company (continued)**

VIII. Repurchases from Employee Stock Ownership Plan Trust

Upon acquisition of shares of stock from participants in the Employee Stock Ownership-Plan in cash settlement of their accounts, the Trust will (1) offer to sell the shares to the Company at the closing market price per share on the New York Stock Exchange on the date of sale and (2) arrange to deliver the shares to Securities Transfer Operation where they will be registered in the name of the Company and forwarded to the bank for custody. The offer will be accepted on behalf of the Company by the Manager-Banking and Corporate Finance in a letter to the Manager-Cash Operations authorizing transfer of funds to the Custodian for the Trust. A copy will be forwarded to the Manager-Accounting Operations for ledger maintenance and reconciliation.

IX. Transfer of Savings and Security, Stock Bonus, and Employee Stock Ownership Plan Trusts

Treasury Operations (Employee Savings Operation) is responsible for administration of these plans. Upon receipt of written requests from Employee Savings Operation, Banking and Corporate Finance will (1) arrange to deliver the requisite number of shares from the custodian to Securities Transfer Operation, (2) issue stock powers authorizing transfer of shares into names designated by Employee Savings Operation, and (3) deliver the re-registered shares into the hands of Trust Investments Operation.

X. Transfers of Shares for Incentive Compensation and Stock-Option Plans

Accounting Services Operation (Personnel Accounting) is responsible for administering these plans. Upon receipt of requests either from Personnel Accounting or Securities Transfer Operation, Banking and Corporate Finance will arrange for (1) delivery of the requisite number of shares from the custodian to Securities Transfer Operation and (2) issuance of necessary stock powers. Securities Transfer Operation will be advised directly by Personnel Accounting concerning re-registration of shares.

XI. Transfer of Shares for Bond Conversions

Foreign Financing is responsible for administering the conversion of these bonds. Upon receipt of requests from that operation, Banking and Corporate Finance will arrange for (1) delivery of the requisite number of shares from the custodian to Securities Transfer Operation and (2) issuance of necessary stock powers.

XII. Record-keeping

Banking and Corporate Finance will maintain a perpetual inventory record of treasury shares. This record will be compared with and reconciled monthly by the Specialist-Corporate Investment to (1) sub-ledger balances maintained by Accounting Operations and (2) custody statements received from the custodian.

# Indirect Repurchasing by or for Employee Benefit Funds

This report has thus far concentrated on direct stock-repurchasing activities by companies that buy their shares in the open market for deposit in the company treasury. The purposes of these acquisitions usually do not include the company holding these treasury shares indefinitely; rather, the shares are intended to be disposed of quite soon for some purpose.

Another aspect of common stock repurchasing, however, often involves substantial numbers of company shares, but these shares are never reported on the corporation's balance sheet as treasury stock. Many corporations operate various types of employee benefit funds such as employee stock-ownership programs, and profit-sharing plans. These funds typically operate as separate entities for accounting purposes. The corporate assets that are turned over to these entities are, therefore, segregated from those of the sponsoring company. A common arrangement is for a corporation that sponsors a pension plan, for instance, to engage a fiduciary agency, such as a bank, to act as trustee for the plan. Periodically, the company deposits cash with the trustee, and the trustee then invests it for the benefit of the covered employees. The cash and/or investments do not appear on the sponsoring company's balance sheet but are accounted for only by the custodian.[6]

These benefit funds must, of course, be invested. And

[6]Under accounting rules presently in effect, sponsors of pension plans are required to make a footnote disclosure of the total amount of such assets that have been set aside to meet their pension obligations.

it is common for the trustees and investment managers of these funds to include varying amounts of shares, depending upon the nature of the benefit program, of the sponsoring company among the investments. Such purchases of company shares are of interest in this study because some of the objectives of direct repurchasing (described earlier in this report) may be attained indirectly through the benefit-plan investment activities.

### Extent of Purchases by Benefit Funds

Sixty-two companies responded to a Conference Board inquiry concerning the investment by their employee benefit funds in the sponsoring companies' common stock. This inquiry was directed to a different sample of firms from that which supplied the data reported in previous sections.

About half the respondents had acquired the company's common stock during the five-year period, 1978 to 1982, for employee benefit-plan investments. Of the 30 companies that replied affirmatively, 27 reported the numbers of shares that were acquired by their benefit funds during this five-year period. Their aggregates were rather substantial and the purchasing activity was quite steady, as the following tabulation shows:

| Year | Aggregate Number of Shares Purchased by 27 Companies |
|---|---|
| 1978 | 3,640,000 |
| 1979 | 5,586,000 |
| 1980 | 5,051,000 |
| 1981 | 5,804,000 |
| 1982 | 4,304,000 |

Twenty-two of the responding companies also provided information about the numbers of their own shares in their benefit plan portfolios at each year end. The median number of shares held increased from 1978 to 1982.

| Number of Shares Held | Number of Companies 1978 | 1982 |
|---|---|---|
| 5,000,001 or more | 5 | 5 |
| 1,000,001-5,000,000 | 5 | 7 |
| 750,001-1,000,000 | 1 | 2 |
| 500,001- 750,000 | 1 | 2 |
| 250,001- 500,000 | 3 | 2 |
| 100,001- 250,000 | 3 | 2 |
| 100,000 or less | 4 | 2 |
| Total Companies | 22 | 22 |
| Total number of shares held by all 22 companies | 112,479,000 | 120,305,000 |

### Types of Benefit Plans

The 30 survey participants that responded affirmatively operate a total of 55 employee benefit plans that invest in varying degrees in the common stock of the sponsoring companies.[1] The various types reported are:

| Type | Number of Plans Reported |
|---|---|
| Employee stock-ownership plans | 19 |
| Employee thrift or savings plans | 17 |
| Profit-sharing plans | 10 |
| Pension plans | 5 |
| Other[1] | 4 |
| Total Plans | 55 |

[1]Includes dividend reinvestment and share-purchase plan, bonus program, stock-option plan, and monthly investment plan.

### Objectives

The companies taking part in this phase of the study repurchase their own stock primarily for purposes that are related to personnel administration goals. Improving employee motivation through ownership interest, retaining valued employees, reducing turnover, and "general corporate purposes" are by far the most important reasons why these firms sponsor such benefit programs as stock-ownership plans, thrift plans, profit-sharing trusts, and pension programs.

For the purposes of this study, however, the objectives that these companies tend to consider secondary are of significant interest because they may confer on the sponsoring companies some of the advantages that are ordinarily associated with direct stock-repurchasing programs, as previously described.

Table 4 summarizes the objectives reported by the 30 companies supplying information on this point. It also shows the participants' ranking of these objectives in terms of their relative importance (1-most important; 2-next in importance; and so on).

### Results

Thirty participants report a high or moderate degree of success as a result of the purchase of company stock by their employee benefit programs. Improving motivation, retaining valued employees, and reducing turnover are highly or moderately successful in well over 90 percent of the responses.

[1]It is not within the scope of this report to examine the characteristics of the various benefit plans for which survey respondents have purchased sponsoring companies' common shares. Further information about such programs is found in the following publications: Linda Wintner, *Employee Buyouts: An Alternative to Plant Closings*. The Conference Board, Research Bulletin No. 140, 1983. Mitchell Meyer, *Profile of Employee Benefits: 1981 Edition*. The Conference Board, Report No. 813, 1981.

**Table 4: Objectives in Stock Repurchasing for Employee Benefit Plans**

| Objectives | Total Mentions (Multiple Responses) | Rank 1 | 2 | 3 | 4 | 5 | 6 | 7 |
|---|---|---|---|---|---|---|---|---|
| | | Number of Ratings | | | | | | |
| *Personnel Relations Objectives:* | | | | | | | | |
| Improve employee motivation through ownership interest | 25 | 19 | 3 | 2 | | 1 | | |
| Retain valued employees | 16 | 3 | 11 | 1 | 1 | | | |
| Reduce general employee turnover | 14 | | 4 | 9 | | | 1 | |
| *Financial Management Objectives:* | | | | | | | | |
| Improve ratio of debt to stockholders' equity | 4 | 1 | 1 | 1 | | 1 | | |
| Prevent unwanted takeovers | 3 | | 1 | 1 | 1 | | | |
| Increase ratio of stockholders' equity to total assets | 4 | 1 | | | | | 2 | 1 |
| Improve effective control by present management | 2 | | | 2 | | | | |
| Increase alternatives available for future capital structure decisions | 2 | | | | 1 | | | 1 |
| Recover shares issued for unsatisfactory acquisitions | 1 | 1 | | | | | | |
| Improve ability to raise capital | 1 | | | | 1 | | | |
| Other includes perceived as good investment; make money buying stock at low price; a good investment for defined benefit master trust; reduce corporate taxes through a Tax Reform Act Stock Ownership Plan (TRASOP) | 5 | 3 | | | 1 | | 1 | |

Results reported in attaining financial management objectives were not so clear-cut. The results of only three financial management objectives were rated by a sufficient number of companies to have any significance: improving ratio of debt to equity, preventing unwanted takeovers, and increasing ratio of equity to assets. From two-thirds to three-quarters of the respondents rate the results for these objectives as highly or moderately successful.

One-fourth of the respondents reporting results believe that they have enjoyed little or no success in improving the ratio of debt to equity. And one out of three report similarly disappointing results in preventing unwanted takeovers and in increasing the ratio of equity to assets. The most likely explanation for these results is that, in many cases, benefit plans cannot buy enough of a sponsoring company's shares to have much effect in pursuing these objectives. Table 5 summarizes these responses.

## Administration

Administration of benefit plans, from the point of view of this study, frequently begins with a board of directors' resolution to allow use of the company's common stock as an investment option in a savings plan or other benefit program. A separate board resolution may be required to allow management to contribute stock to the employee benefit trust up to a specified limit.

Where purchasing of company stock is authorized as an investment of benefit plan assets, more than seven out of ten survey participants make such purchases on a continuing basis. The most common practice is to buy the shares through stockbrokers; but it is not unusual to make such purchases through a bank. The following tabulation summarizes the practices of responding companies in acquiring sponsoring companies' shares for benefit funds:

| Method Used to Acquire Shares | Number of Responses[1] |
|---|---|
| Purchases through brokers | 20 |
| Purchases through banks that obtain shares through brokers of their own choice | 12 |
| Issuance of new shares by the company | 9 |
| Direct purchases of shares offered by individuals or by holders of large blocks of stock | 3 |
| Purchases from employees who acquired shares through savings plans or other such programs | 3 |
| Purchases by trustee | 1 |

[1]Mutiple responses.

Slightly less than half of the participants have some

**Table 5: Achievement of Objectives**

| Objectives | Degree of Success Reported (Percent of Responses) High | Moderate | Little or None |
|---|---|---|---|
| *Personnel Relations Objectives:* | | | |
| Improve motivation through ownership | 32% | 64% | 4% |
| Retain valued employees | 38 | 56 | 6 |
| Reduce turnover | 14 | 79 | 7 |
| *Financial Management Objectives:* | | | |
| Improve ratio of debt to equity | | 75 | 25 |
| Prevent unwanted takeovers | 33 | 33 | 34 |
| Increase ratio of equity to assets | 33 | 33 | 34 |

kind of written guidelines for the acquisition of company stock by benefit plans. The board resolutions noted above are common examples. One company reports that its board of directors makes an annual review of the investment decisions made by or for benefit funds.

In cases where directors' resolutions or policy statements are used, they may (1) refer to SEC rules concerning market purchases, (2) specify who is to carry out or delegate execution of such purchases, (3) provide guidelines regarding pooling of trust funds assets, (4) specify when and to what extent company stock shall be used in investment of assets, and (5) establish general investment standards including types of assets eligible for inclusion in trustee-supervised funds.